

O

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

VELTEX CORPORATION,

Plaintiff,

v.

JAVEED AZZIZ MATIN, et al.,

Defendants.

CV 10-1746 ABC (PJWx)

ORDER GRANTING MOTIONS TO
DISMISS

Pending before the Court are motions to dismiss filed by Defendants Carmine Bua ("Bua"), Chisholm, Bierwolf, Nilson & Morrill, CPA ("CBNM"), Anne Tahim ("Tahim"), Patrick Day, Richard Day, and American Registrar and Transfer Co. ("ARTCO") (collectively, "Defendants"). (See Bua Mot. (Docket # 125); CBNM Mot. (Docket # 126); Tahim Mot. (Docket # 124); Patrick Day, Richard Day & ARTCO Mot. ("Day Mot.") (Docket # 122).) Plaintiff filed oppositions. (Opp'n to Bua Mot. (Docket # 129); Joint Opp'n to CBNM and Tahim Mots. ("Joint Opp'n") (Docket # 131); Opp'n to Patrick Day, Richard Day & ARTCO Mot. ("Opp'n to Day Mot.") (Docket # 133).) Defendants filed replies. (Bua Reply (Docket # 138); CBNM Reply (Docket # 140); Tahim Reply (Docket # 139); Patrick Day, Richard Day & ARTCO Reply ("Day Reply")

(Docket # 137).) The motions came on for hearing on September 27, 2010. Having reviewed the parties' arguments and the record, the Court hereby **GRANTS** the motions.

I. BACKGROUND

This is a securities fraud case in which Plaintiff alleges that various defendants engaged in a "pump and dump" scheme to artificially inflate the value of Veltex stock by disseminating false information and then sell the inflated shares into the market. (See, e.g., First Amended Complaint ("FAC") ¶ 1.) Plaintiff Veltex is an apparel company that claims that it was a victim of this scheme along with unsuspecting investors. (FAC ¶¶ 1, 4.) Plaintiff alleges that the pump and dump scheme "required planning and numerous participants, including lawyers, accountants and transfer agents." (FAC ¶ 1.) Some of those defendants are currently before the Court with pending motions to dismiss.

Defendant Bua acted as Plaintiff's securities attorney. (See FAC ¶ 25.) Plaintiff alleges that Bua rendered fraudulent opinion letters ("Rule 504D Letters") approving the issuance of legend free shares of Veltex stock. (See, e.g., FAC ¶¶ 25, 68-69, 71.) Defendant CBNM is a certified public accounting firm that performed accounting work and consulting services for Plaintiff. (FAC ¶ 21.) Plaintiff alleges that CBNM's audit was faulty in various respects. (See, e.g., FAC ¶¶ 51-56.) Defendant Tahim is a certified public accountant who performed accounting work for Plaintiff. (FAC ¶ 23.) Plaintiff alleges that Tahim's audit was faulty in various respects. (See, e.g., FAC ¶¶ 49-50.) Defendant ARTCO is a corporate transfer agent engaged in facilitating the registry and transfer of corporate shares.

1 (FAC ¶ 16.) Defendant Patrick Day was the President of ARTCO during
2 certain periods, and was also a member of Plaintiff's Board of
3 Directors. (FAC ¶ 17.) Defendant Richard Day held a variety of
4 management positions with ARTCO and was a majority owner of ARTCO.
5 (FAC ¶ 18.) Plaintiff alleges that ARTCO, Patrick Day and Richard Day
6 improperly issued legend free shares of Veltex stock. (See FAC ¶ 72.)
7 Plaintiff also alleges that the various defendants in Plaintiff's
8 management, apparently including Patrick Day, engaged in various other
9 misconduct. (See, e.g., FAC ¶¶ 32-34.)

11 II. STANDARDS

12 Defendants move for dismissal pursuant to Federal Rule of Civil
13 Procedure 12(b)(6) on the ground that Plaintiff failed to state a
14 claim upon which relief can be granted. The Supreme Court has
15 recently clarified the pleadings necessary to state a claim for relief
16 sufficiently to withstand a motion to dismiss under Rule 12(b)(6).
17 See Ashcroft v. Iqbal, __ U.S. ___, 129 S. Ct. 1937 (2009); Bell Atl.
18 Corp. v. Twombly, 550 U.S. 544 (2007). Rule 8(a)(2) requires a "short
19 plain statement of the claim showing that the pleader is entitled to
20 relief," which does not require "detailed factual allegations," but it
21 "demands more than an unadorned, the-defendant-unlawfully-harmed-me
22 accusation." Iqbal, 129 S. Ct. at 1949. A claim must be "plausible
23 on its face," which means that the Court can "draw the reasonable
24 inference that the defendant is liable for the misconduct alleged."
25 Id. In other words, "a plaintiff's obligation to provide the grounds
26 of his entitlement to relief requires more than labels and
27 conclusions, and a formulaic recitation of the elements of a cause of
28 action will not do." Twombly, 550 U.S. at 555 (internal quotations

1 and alterations omitted). Allegations of fact are taken as true and
 2 construed in the light most favorable to the nonmoving party. See,
 3 e.g., Newdow v. Lefevre, 598 F.3d 638, 642 (9th Cir. 2010).¹

4 If the court finds dismissal appropriate, it must decide whether
 5 to grant leave to amend. Leave to amend under Rule 15(a) is "freely
 6 given when justice so requires." In the Ninth Circuit, "[t]his policy
 7 is 'to be applied with extreme liberality.'" Eminence Capital, LLC v.
 8 Aspeon, Inc., 316 F.3d 1048, 1051 (9th Cir. 2003) (per curiam)
 9 (quoting Owens v. Kaiser Found. Health Plan, Inc., 244 F.3d 708, 712
 10 (9th Cir. 2001)). Dismissal without leave to amend is improper unless
 11 it is clear that the complaint cannot be saved by any amendment.
 12 Polich v. Burlington Northern, Inc., 942 F.2d 1467, 1472 (9th Cir.
 13 1991). Where the plaintiff makes a bare request for leave to amend
 14 unaccompanied by additional facts that could cure the defects in the
 15 complaint, however, that is a strong indication that the plaintiff has
 16 no additional facts to plead. See In re Vantive Corp. Securities
 17 Litig., 283 F.3d 1079, 1098 (9th Cir. 2002), abrogation on other
 18 grounds recognized by South Ferry LP, No. 2 v. Killinger, 542 F.3d
 19 776, 784 (9th Cir. 2008). Moreover, the Court's discretion is
 20 particularly broad in cases where leave to amend has been granted
 21 previously. See Metzler Inv. GmbH v. Corinthian Colleges, Inc., 540
 22 F.3d 1049, 1071 (9th Cir. 2008).²

25 ¹ As discussed more fully below, some of Plaintiff's claims are
 26 subjected to heightened pleading standards.

27 ² Plaintiff previously requested - and was granted - leave to
 28 amend with respect to Defendants Bua, Tahim, and CBNM. (See June 28,
 2010 Tr. at 14-18.)

1 **III. ANALYSIS**

2 Defendants' pending motions raise a variety of arguments that
3 they assert warrant dismissal of various of the claims asserted. The
4 Court addresses each below.

5 **A. First Cause of Action - § 12 Claim**

6 The FAC raises a claim under § 12 of the Securities Act of 1933.
7 (See FAC ¶ 85.) That section provides that any person who "offers or
8 sells a security" by means of untrue statements is liable "to the
9 person purchasing such security from him." 15 U.S.C. § 771(a).
10 Hence, § 12 "permits suit against a seller of a security . . . only by
11 'the person purchasing such a security from him,' thus specifying that
12 a plaintiff must have purchased the security directly from the
13 issuer." Hertzberg v. Dignity Partners, Inc., 191 F.3d 1076, 1081
14 (9th Cir. 1999) (emphasis in original). This poses two problems for
15 Plaintiff. First, Plaintiff has not alleged that it actually
16 purchased securities at all, which makes its claim as currently pled
17 defective as to all Defendants. Plaintiff contends that it in fact
18 did make at least one such purchase, however. (Peters Decl. ¶ 8, Ex.
19 F.) Accordingly, with respect to that defect, this claim is **DISMISSED**
20 without prejudice as to all moving Defendants. If Plaintiff amends
21 this claim, it should specify which of the remaining Defendants sold
22 securities to Veltex.

23 Second, Tahim argues that Plaintiff did not purchase any
24 securities from her as required under § 12. (See Tahim Mot. at 10.)
25 The Ninth Circuit has made clear that an accountant "merely performing
26 professional services, without actively soliciting a purchase of the
27 underlying securities, does not give rise to liability under section
28 12." Moore v. Kayport Package Exp., Inc., 885 F.2d 531, 537 & n.5

(9th Cir. 1989); see also In re: Worlds of Wonder Securities Litig., 694 F. Supp. 1427, 1435 (N.D. Cal. 1988) (dismissing claims against accountants who finalized registration statement and prospectus and caused registration statement to become effective). Plaintiff fails to address this authority in opposition, and instead notes that claims against accountants are not categorically barred. (See Joint Opp'n at 18-19.) But Plaintiff does not provide an explanation why the particular allegations against this accountant pass muster under Ninth Circuit law. Accordingly, this claim is **DISMISSED** with prejudice as to Tahim.

B. First Cause of Action - § 17(a) Claim

The FAC raises a claim under § 17(a) of the Securities Act of 1933. (See FAC ¶ 85.) This claim fails as a matter of law because there is no private right of action under § 17(a). In re Washington Public Power Supply Sys. Sec. Litig., 823 F.2d 1349, 1358 (9th Cir. 1987) (en banc) ("no private right of action lies under section 17(a)"). That claim is **DISMISSED** with prejudice against all moving Defendants.

C. First Cause of Action - § 10b-5, Rule 10(b)-5 Claim

To state a claim under § 10(b) and Rule 10b-5, a plaintiff must allege: (1) a misstatement or omission (2) of material fact (3) made with scienter (4) on which the plaintiff relied (5) which proximately caused its injury. DSAM Global Value Fund v. Altris Software, Inc., 288 F.3d 385, 388 (9th Cir. 2002) Such claims are subject to heightened pleading requirements. Federal Rule of Civil Procedure 9(b) requires allegations of fraud be pled with particularity. See, e.g., Desaiqoudar v. Meyercord, 223 F.3d 1020, 1023 (9th Cir. 2000).

The Private Securities Litigation Reform Act of 1995 ("PSLRA")

1 modifies Rule 9(b) to add further pleading requirements for securities
2 claims. See id. The PSLRA was designed to eradicate "pleading fraud
3 by hindsight." In re: Daou Sys., Inc., 411 F.3d 1006, 1021 (9th Cir.
4 2005). "Under the PSLRA's heightened pleading instructions, any
5 private securities complaint alleging that the defendant made a false
6 or misleading statement must: (1) specify each statement alleged to
7 have been misleading and the reason or reasons why the statement is
8 misleading; and (2) state with particularity facts giving rise to a
9 strong inference that the defendant acted with the required state of
10 mind." Tellabs, Inc. v. Makor Issues & Rights, Ltd., 551 U.S. 308,
11 321 (2007) (internal citations and quotations omitted). The Ninth
12 Circuit has traditionally analyzed these overlapping issues as a
13 single inquiry. See, e.g., Ronconi v. Larkin, 253 F.3d 423, 429 (9th
14 Cir. 2001). The Court therefore must determine whether "particular
15 facts in the complaint, taken as a whole, raise a strong inference
16 that defendants intentionally or [with] 'deliberate recklessness' made
17 false or misleading statements to investors." Id.

18 The Supreme Court has provided guiding principles in determining
19 whether that pleading standard has been met. First, the Court is to
20 accept all factual allegations as true. Tellabs, 551 U.S. at 322.
21 Second, the Court must look to the allegations in the complaint in
22 their entirety. Id. Third, the court must take into account
23 plausible competing inferences. Id. at 323. "A complaint will
24 survive . . . only if a reasonable person would deem the inference of
25 scienter cogent and at least as compelling as any opposing inference
26 one could draw from the facts alleged." Id. at 324.

27 1. Bua

28 Bua's challenge to the sufficiency of the FAC focuses on whether

1 Plaintiff sufficiently pled scienter. (See Bua Mot. at 7-11.)
 2 Plaintiff alleges that Bua drafted at least 33 Rule 504D Letters
 3 approving the issuance of unrestricted, legend free Veltex common
 4 stock. (FAC ¶ 69.)³ Plaintiff argues that no securities law
 5 exemption was available, and that the Rule 504D Letters were premised
 6 on misrepresentations that Wilshire Equity was a Texas resident and
 7 that Veltex, Javeed Matin ("Matin") and Wilshire Equity were
 8 unaffiliated. (See Opp'n to Bua Mot. at 4-8, 12; see also FAC ¶ 71.)⁴
 9 Plaintiff argues that, despite receiving these facts from Matin and
 10 others at Veltex, Bua actually knew, or with deliberate recklessness
 11 disregarded, that his Rule 504D Letters were false. (See Opp'n to Bua
 12 Mot. at 12; see also FAC ¶ 71(a).)⁵

13
 14 ³ Bua was compensated up to \$1,000 for each of the letters.
 (FAC ¶ 69.)

15 ⁴ Matin was the CEO and Chairman of the Board of Veltex. (FAC ¶
 16 5.) Wilshire Equity "was the vehicle that received the inflated,
 17 unrestricted and legend free Veltex common stock shares which were
 18 then sold to unsuspecting investors through several smaller, regional
 19 brokerage accounts in California and in Utah." (FAC ¶ 66.) Plaintiff
 20 alleges that, "[b]ecause Wilshire Equity was wholly owned by Matin,
 21 who was also CEO and Chairman of the Board of Veltex, he was deemed to
 be an 'affiliate' of Veltex, and under applicable law . . . the Veltex
 shares transferred to Wilshire were required to bear a restrictive
 legend by the transfer agent at the time the shares were issued,
 unless an attorney certifies that under Regulation D, Rule 504 . . . ,
 the proposed shares are 'legend free shares.'" (FAC ¶ 67.)

22 ⁵ The parties differ in their categorization of Plaintiff's
 23 claim. Bua views the claim as being based on his issuance of a false
 24 or misleading statement. (See Reply at 5 ("The claim must be pled
 25 with specific facts to show a defendant made a false or misleading
 26 statement and the defendant had the requisite scienter when he made
 27 such statement.")) Plaintiff views the claim as arising under a
 28 "scheme liability" theory. (Opp'n to Bua Mot. at 11.) A defendant
 may be liable under a "scheme liability" theory where he engaged in a
 deceptive act as part of a larger scheme to defraud the securities
 market where that act has the principal purpose and effect of creating
 a false appearance of fact in furtherance of the scheme. See, e.g.,
Burnett v. Rowzee, 561 F. Supp. 2d 1120, 1125 (C.D. Cal. 2008). The

1 "An attorney who undertakes to make representations to
 2 prospective purchasers of securities is under an obligation, imposed
 3 by Section 10(b), to tell the truth about those securities." Thompson
 4 v. Paul, 547 F.3d 1055, 1063 (9th Cir. 2008). Of course, those
 5 attorneys must have the requisite scienter to be held liable.
 6 Scienter exists where there is "a highly unreasonable omission,
 7 involving not merely simple, or even inexcusable negligence, but an
 8 extreme departure from the standards of ordinary care." DSAM Global
 9 Value Fund, 288 F.3d at 389 (quoting Hollinger v. Titan Capital Corp.,
 10 914 F.2d 1564, 1569 (9th Cir. 1990)). The Third Circuit has found
 11 that a lawyer's reliance on information provided by his client and
 12 failure to investigate is probative of scienter only where he knows or
 13 has good reason to know that the facts provided are inaccurate. See
 14 Kline v. First Western Government Sec., Inc., 24 F.3d 480, 486 (3d
 15 Cir. 1994) ("When the opinion . . . is based on underlying materials
 16 which on their face or under the circumstances suggest that they
 17 cannot be relied upon without further inquiry, then the failure to
 18 investigate further may 'support an inference that when the defendant
 19 expressed the opinion it had no genuine belief that it had the
 20 information on which it could predicate that opinion.'" (quoting
 21 Eisenberg v. Gagnon, 766 F.2d 770, 776 (3d Cir. 1985))).

22 Plaintiff has not met that standard. For example, Plaintiff
 23 alleges that "Bua knew, or consciously and recklessly disregarded" the
 24 affiliate relationship between Veltex, Matin and Wilshire Equity.
 25 (See FAC ¶ 71(a).) Plaintiff argues that such scienter can be

26 _____
 27 parties do not delineate any difference in the scienter requirement
 28 between the two types of claims, and the Court deciphers none. (See
 June 25, 2010 Minute Order at 4 n.2.)

1 inferred because Bua had good reason to distrust his client's contrary
2 representations in light of the similarities in the signatures on
3 Bua's paychecks from Veltex and the signature on behalf of Wilshire
4 Equity on Securities Purchase Agreements. (See FAC ¶ 71(a).)⁶ It is
5 theoretically possible that an attorney may have recognized the
6 similarity in signatures on these unrelated documents. But Plaintiff
7 fails to provide authority that attorneys are expected to sleuth
8 through seemingly unrelated documents in an attempt to detect
9 inaccuracy in facts provided by their clients.⁷

10 With respect to the alleged misrepresentation that Wilshire
11 Equity was a Texas resident, Bua issued a letter advising that
12 Pennsylvania law had been reinterpreted to provide stricter legend
13 requirements, making Texas law more favorable. (See FAC ¶ 71(f), Ex.
14 41.) While Plaintiff points to the fact that Bua's subsequent Rule
15 504D Letters switched Wilshire Equity from a Pennsylvania to a Texas
16 resident, Plaintiff fails to consider the plausible inference that Bua
17 believed Wilshire Equity actually became a Texas resident in response
18 to his opinion that Texas law was more beneficial than Pennsylvania
19

20 ⁶ These were not Martin's signatures, but allegedly the signature
21 of Mazhar Haque. (FAC ¶ 71(a).) His name is not typed on the
signature page. (See FAC Exs. 36-37.)

22 ⁷ Nor does the Court find persuasive Plaintiff's allegation that
23 Bua was put on notice by Richard Day of unrelated errors in his
24 letters. There is no indication that Bua failed to correct any errors
25 identified or that he was provided notice that any of the alleged
misrepresentations at issue in the pending motion were inaccurate.
26 Plaintiff's opposition indicates that Bua was "frequently" notified of
inaccuracies in his Rule 504D Letters. (See Opp'n to Bua Mot. at 18.)
27 Of the allegedly 33 or more Rule 504D Letters drafted by Bua for
Veltex, Plaintiff identified two instances of inaccuracies being
28 pointed out to him. (See FAC ¶¶ 69, 71(b), 71(c).) Plaintiff also
alleges an instance in which Bua provided an explanation to Richard
Day as to the basis of his opinion. (See FAC ¶ 71(e).)

1 law. Tellabs, 551 U.S. at 324 (scienter is sufficiently alleged "only
2 if a reasonable person would deem the inference of scienter cogent and
3 at least as compelling as any opposing inference one could draw from
4 the facts alleged." (emphasis added).) Plaintiff fails to adequately
5 explain why Bua should have doubted that Wilshire Equity actually
6 became a Texas resident after he had opined that Texas law was more
7 beneficial.⁸

8 The ultimate question on a motion to dismiss is whether the
9 allegations as a whole, including even vague and ambiguous
10 allegations, raise a strong inference of scienter. South Ferry, 542
11 F.3d at 784. While the FAC moved Plaintiff closer to raising a strong
12 inference of scienter, taking the FAC's allegations as a whole it
13 still fails to do so. The Court will therefore allow Plaintiff one
14 further opportunity to allege this claim against Bua in accord with
15 the pleading requirements of the PSLRA. This claim against Bua is
16 **DISMISSED** with leave to amend.

17 2. CBNM

18 CBNM's challenge to the sufficiency of the FAC focuses on whether
19 Plaintiff sufficiently pled falsity or scienter. (CBNM Mot. at 2-5.)
20 Plaintiff alleges that CBNM was hired in September 2004 by Veltex to
21 perform an audit for its financial statements as of December 31, 2003.
22 (FAC ¶ 52.) CBNM did in fact perform that audit. (FAC ¶ 52, Ex. 30.)
23

24 ⁸ Indeed, Plaintiff provides little factual support for its
25 apparent contention that Wilshire Equity was not actually a Texas
26 resident at that time. Plaintiff states in a footnote that Wilshire
27 Equity shared the same Texas address as other entities who were issued
28 Veltex unrestricted shares. (See Opp'n to Bua Mot. at 6 n.7; FAC ¶
71(g).) Plaintiff failed to sufficiently explain why this allegation
shows that Wilshire Equity was not a Texas resident and/or why it
supports an inference of scienter.

1 Plaintiff does not allege that any of the financial information in the
2 financial statements audited by CBNM was false. For example, CBNM
3 reported that the financial statements accurately reflected that
4 Veltex had a net loss of \$1.8 million. (See FAC Ex. 30.) Plaintiff
5 does not dispute the accuracy of that figure.

6 Instead, Plaintiff argues that CBNM "falsely represented" that it
7 had complied with accepted auditing standards when, in fact, it had
8 not. (See Joint Opp'n at 10.) Plaintiff failed to sufficiently
9 explain why an outside auditor can be held liable for securities fraud
10 based solely on its failure to comply with accounting standards when
11 that failure in no way impacted the substance of the financial
12 information at issue. While those allegations may show that CBNM
13 failed to competently perform its audit as represented, Plaintiff
14 fails to show that they state a claim for securities fraud.

15 Moreover, Plaintiff failed to sufficiently plead scienter. As
16 noted above, scienter exists where there is "a highly unreasonable
17 omission, involving not merely simple, or even inexcusable negligence,
18 but an extreme departure from the standards of ordinary care." DSAM
19 Global Value Fund, 288 F.3d at 389. In analyzing the scienter of
20 auditors, the Ninth Circuit has articulated a very high standard:

21 [T]he mere publication of inaccurate accounting
22 figures, or a failure to follow GAAP, without more,
23 does not establish scienter. Rather, scienter requires
24 more than a misapplication of accounting principles.
25 The plaintiff must prove that the accounting practices
26 were so deficient that the audit amounted to no audit
at all, or an egregious refusal to see the obvious, or
to investigate the doubtful, or that the accounting
judgments which were made were such that no reasonable
accountant would have made the same decisions if
confronted with the same facts.

27 DSAM Global Value Fund, 288 F.3d at 390 (quoting In re Software
28 Toolworks, Inc., 50 F.3d 615, 627-28 (9th Cir. 1994)). Plaintiffs

1 "must allege enough information so that a court can discern whether
2 the alleged GAAP violations were minor or technical in nature, or
3 whether they constituted widespread and significant inflation of
4 revenue." Daou Systems, 411 F.3d at 1017 (internal quotations
5 omitted). In this case, Plaintiff lists alleged accounting violations
6 unaccompanied by any inflation in the revenue figures provided by
7 CBNM. This is not sufficient to plead scienter.

8 For these reasons, Plaintiff failed to sufficiently plead this
9 claim against CBNM.⁹ Accordingly, because Plaintiff has previously
10 amended the complaint as to CBNM, this claim against CBNM is **DISMISSED**
11 with prejudice.

12 3. Tahim

13 Plaintiff alleges that Tahim violated the securities laws by
14 issuing an audit report that failed to conform with GAAP standards and
15 was substantially deficient. (See Joint Opp'n at 7.) Tahim argues as
16 a threshold matter that the claim is untimely. (Tahim Mot. at 3-4.)
17 Claims for security fraud must be brought no later than the earlier of
18 (1) two years after the discovery of the facts constituting the
19 violation; or (2) five years after such violation. 28 U.S.C. §
20 1658(b). Thus, the securities laws include both a two-year statute of
21 limitations (subject to tolling principles) and a five-year statute of
22 repose (not subject to tolling principles). See Lampf, Pleva,

23
24 ⁹ Plaintiff also argues that CBNM may be liable under a scheme
25 liability theory. (See Joint Opp'n at 15-16.) As noted above, scheme
26 liability requires allegations of a deceptive act as part of a larger
27 scheme to defraud the securities market where that act has the
28 principal purpose and effect of creating a false appearance of fact in
furtherance of the scheme. Burnett, 561 F. Supp. 2d at 1125.
Plaintiff has failed to allege with specificity an actionable
deceptive act purportedly engaged in by CBNM. Plaintiff also failed
to allege sufficient facts supporting a strong inference of scienter.

1 Lipkind, Prupis & Petigrow v. Gilbertson, 501 U.S. 350, 363 (1991).

2 Here Plaintiff alleges that Tahim issued her audit report on January
3 6, 2004. (FAC ¶ 49.) The Complaint was filed more than six years
4 later, on March 10, 2010. (Complaint (Docket # 1).)¹⁰

5 Plaintiff's opposition ignores Tahim's argument that the claim is
6 barred by the five-year repose provision. (See Joint Opp'n at 16
7 (addressing only the two-year statute of limitations, not the five-
8 year statute of repose).) The five-year statute of repose begins to
9 run on the date of the alleged false representation. In re Juniper
10 Networks, Inc. Sec. Litig., 542 F. Supp. 2d 1037, 1051 (N.D. Cal.
11 2008); see also Lampf, 501 U.S. at 364 (calculating repose period from
12 date of alleged misrepresentations). Each false statement constitutes
13 a separate violation, so the five-year period runs separately for each
14 violation when it occurs. Juniper, 542 F. Supp. 2d at 1051 (citing In
15 re Zoran Corp. Derivative Litig., 511 F. Supp. 2d 986, 1014 (N.D. Cal.
16 2007)). Plaintiffs may not recover for alleged misrepresentations
17 made prior to the five-year period under a theory of a continuing
18 wrong. Id. Accordingly, on its face, the FAC's allegation of
19 wrongdoing by Tahim is untimely, and Plaintiff provided no reason to
20 find otherwise. Nor does Plaintiff identify any factual allegations
21 that could be made to make the claim timely. Accordingly, because
22 Plaintiff cannot amend to avoid the five-year statute of repose, this
23 claim against Tahim is **DISMISSED** with prejudice.

24 4. Richard Day, Patrick Day and ARTCO

25 Richard Day, Patrick Day and ARTCO (collectively, the "Day
26

27 ¹⁰ By March 10, 2005 (five years before the filing of the
28 complaint), CBNM was responsible for auditing Plaintiff. (See, e.g.,
FAC ¶¶ 48(n), 51-52.)

1 Defendants") also move to dismiss the § 10 claim brought against them.
2 The Day Defendants' alleged involvement in the securities scheme
3 differs from the accountant and attorney Defendants discussed above.
4 Plaintiff alleges that ARTCO, Patrick Day and Richard Day issued
5 legend free shares of Veltex stock:

6 ARTCO, which operated as Veltex' [sic] share transfer
7 agent, financially benefitted from each such transfer
8 it effected. Defendant Patrick Day, who is the
9 President of ARTCO (and whose father, Richard Day, is
10 the majority owner of ARTCO, and had been one of
11 Veltex's outside securities attorneys), was also a
12 Director of Veltex at the same time ARTCO served as
13 Veltex' [sic] share transfer agent. Upon receipt of
14 the "authorization letter" from Matin or other of the
Management Defendants, ARTCO would then issue the
legend free and unrestricted shares to Wilshire Equity
or one of the other entities, and they would be sold
directly on the open market to unsuspecting members of
the general investing public, or in turn transferred to
other nominees controlled by Matin and the other
Management Defendants, who then sold them to the
public.

15 (FAC ¶ 72; see also FAC ¶¶ 16-18.) Although not specified by name,
16 Plaintiff also alleges that the various defendants in Plaintiff's
17 management, including Patrick Day, engaged in various other
18 misconduct. (See, e.g., FAC ¶¶ 32-34.) Plaintiff also alleges that
19 Richard Day contacted Bua on at least three occasions to point out
20 inaccuracies in his Rule 504D Letters or request an explanation for
21 the basis of Bua's opinion. (See FAC ¶¶ 71(b), (c), (e).)

22 As with the accountants and attorney Defendants, the Day
23 Defendants argue that the § 10 claim against them has not been
24 sufficiently pled under the PSLRA.

25 a. Patrick Day

26 Plaintiff argues that liability attaches for Patrick Day based on
27 material misrepresentations and omissions in press releases and other
28 statements issued while he was a board member of Veltex. (See Opp'n

1 to Day Mot. at 14.) Patrick Day's motion challenges, inter alia, the
2 sufficiency of the FAC's allegations on scienter. Plaintiff argues
3 that Patrick Day "was able to, and did, control the content" of those
4 press releases and other statements. (See id.) Plaintiff cites for
5 support of that proposition its allegation that all "Management
6 Defendants, because of their positions as Officers and/or Directors of
7 Veltex, were able to, and did, control the content of press releases
8 and other public statements pertaining to Veltex." (FAC ¶ 2; Opp'n to
9 Day Mot. at 6.)

10 Even assuming such a fact was pled sufficiently, Plaintiff failed
11 to properly plead scienter. Plaintiff argues a strong inference of
12 scienter exists because Patrick Day was a Director of Veltex and
13 President of ARTCO, so he was involved "in the day-to-day operations
14 of both." (Opp'n to Day Mot. at 16.) "Where a complaint relies on
15 allegations that management had an important role in the company but
16 does not contain additional detailed allegations about the defendants'
17 actual exposure to information, it will usually fall short of the
18 PLSRA standard." South Ferry, 542 F.3d at 784. "As a general matter,
19 'corporate management's general awareness of the day-to-day workings
20 of the company's business does not establish scienter-at least absent
21 some additional allegation of specific information conveyed to
22 management and related to the fraud' or other allegations supporting
23 scienter." Id. at 784-85. That type of additional allegation has not
24 been pled in the FAC.

25 As an initial matter, Plaintiff failed to identify detailed
26 factual allegations showing that Patrick Day had an awareness of the
27 day-to-day operation of Veltex. Even assuming that fact was
28 sufficiently pled in the FAC, however, it is not sufficient to

1 establish scienter under the PSLRA because the FAC does not include
2 additional allegations showing information conveyed to Patrick Day
3 concerning the fraud or other allegations supporting scienter.

4 Accordingly, this claim against Patrick Day is **DISMISSED** without
5 prejudice.

6 c. Richard Day

7 Plaintiff's opposition asserts that Richard Day made material
8 omissions in authorizing the improper issuance of millions of shares
9 of Veltex stock without a restrictive legend based on Bua's erroneous
10 Rule 504D Letters. (See Opp'n to Day Mot. at 14-15.) With respect to
11 Richard Day's scienter, Plaintiff argues that a strong inference
12 arises because (1) he corrected some errors in Bua's Rule 504D Letters
13 and (2) he served as a securities attorney for Veltex in 2006. (See
14 id. at 16.) Plaintiff infers from these facts that Richard Day knew
15 of the alleged fraud and had contacted Bua to ensure that the Rule
16 504D Letters were free from glaring defects "in an effort to make
17 ARTCO's distribution of Veltex stocks appear legitimate." (See id. at
18 7.) Plaintiff ignores the competing, plausible inference that Richard
19 Day informed Bua of inaccuracies in his letters because he wanted and
20 expected the letters on which he relied to be accurate.

21 As the Supreme Court has recognized, the Court does not determine
22 the strength of inferences in a vacuum without considering plausible,
23 nonculpable explanations for a defendant's conduct. Tellabs, 551 U.S.
24 at 323-24. Plaintiff fails to explain why its nefarious inference is
25 as least as compelling as the harmless competing inference.
26 Considering all of the allegations in the FAC, the Court does not
27 believe that Plaintiff's inference is as compelling and, therefore,
28 finds Richard Day's scienter to be insufficiently pled. Id. at 324

1 (scienter is sufficiently alleged "only if a reasonable person would
2 deem the inference of scienter cogent and at least as compelling as
3 any opposing inference one could draw from the facts alleged."

4 (emphasis added).)

5 Accordingly, the Court **DISMISSES** without prejudice this claim
6 against him.¹¹

7 d. ARTCO

8 Plaintiff does not identify any basis to hold ARTCO liable
9 separate from the allegations against Patrick and Richard Day. (See,
10 e.g., Opp'n to Day Mot. at 14-15 (analyzing purported
11 misrepresentations and omissions of Richard and Patrick Day with no
12 reference to other factual allegations concerning ARTCO).)
13 Accordingly, the claim against ARTCO fails for the reasons identified
14 above and is **DISMISSED** without prejudice.¹²

15 **D. Sixth and Seventh Causes of Action**

16 CBNM and Tahim request that the Court dismiss the California
17 state law claims against them. (CBNM Mot. at 10-11; Tahim Mot. at

18 ¹¹ Plaintiff lastly alleges that it sufficiently pled scheme
19 liability as to the Day Defendants based on the allegations discussed
20 above, as well as the allegation that Patrick Day signed two
21 authorizations for the issuance of shares of Veltex stock pursuant to
22 Rule 504D. (See Opp'n to Day Mot. at 11; FAC Ex. 34 at 200, 219.) As
23 Plaintiff acknowledges, a scheme liability claim requires a showing of
24 scienter, among other elements. (See Opp'n to Day Mot. at 12 n.3.)
25 Scienter has not been sufficiently pled.

26 ¹² The Court notes that some of Plaintiff's arguments regarding
27 the Day Defendants are based on facts not contained in the FAC but
28 purportedly supported by evidence provided in declaration form. The
Day Defendants call into doubt the veracity of some of that evidence
by, for example, noting that some of the documents appear to have been
forged or altered. The Court expresses no opinion at this time
regarding these additional factual allegations and accompanying
evidentiary support. In light of the Court's granting Plaintiff leave
to amend, however, the Court reminds Plaintiff of its Rule 11(b)
obligations with respect to any new allegations pled.

12.) The Court may decline to exercise supplemental jurisdiction over state claims following dismissal of all federal claims. See 28 U.S.C. § 1367(c).

With respect to Tahim, the Court has dismissed all federal claims against her with prejudice and declines to exercise supplemental jurisdiction as to the state law claims against her. Accordingly, the state law claims against Tahim are **DISMISSED** without prejudice.

With respect to CBNM, the Court did not dismiss the § 12 claim against CBNM with prejudice. Accordingly, the Court finds its request to dismiss the state law claims on this ground premature. The Court defers ruling on this argument until such time as Plaintiff pleads a viable federal claim against CBNM or the Court dismisses the federal claims against CBNM with prejudice.¹³

IV. CONCLUSION

For the reasons stated above, the pending motions to dismiss are **GRANTED**. The § 12 claim is dismissed without prejudice as to Bua, CBNM, Patrick Day, Richard Day and ARTCO, and is dismissed with prejudice as to Tahim. The § 17(a) claim is dismissed with prejudice as to all moving Defendants. The § 10 claim is dismissed without prejudice as to Bua, Patrick Day, Richard Day and ARTCO, and is dismissed with prejudice as to Tahim and CBNM. The state law claims against Tahim are dismissed without prejudice.

¹³ CBNM also substantively challenges the sufficiency of the allegations to state claims under state law. (CBNM Mot. at 6-10.) The Court will rule on these arguments only if Plaintiff has sufficiently pled a federal claim against CBNM or if the Court determines that it should exercise supplemental jurisdiction over these state law claims despite the absence of a federal claim.

1 Any amended complaint must be filed no later than **October 18,**
2 **2010.**¹⁴

3
4 **IT IS SO ORDERED.**

5
6 **DATED: 9/27/10**



7
8 **AUDREY B. COLLINS**

9 **CHIEF UNITED STATES DISTRICT JUDGE**
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24

25
26 ¹⁴ In its reply brief, CBNM requests that the Court make
27 findings regarding compliance with Rule 11(b). (CBNM Reply at 12.)
28 As this was raised for the first time in reply, the Court does not
rule on it now. Moreover, CBNM's request appears premature as the
statute indicates that such findings should be made "upon final
adjudication of the action." 15 U.S.C. 78u-4(c)(1).